UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

CAPITOL SPECIALTY INSURANCE CORPORATION, Plaintiff, vs. CHARACTERS FOR HIRE, LLC; NICK SARELLI, a/k/a Avi Lieberman, d/b/a Characters for Hire, LLC; and ABC CORPORATIONS 1-10 (individual fictitious corporate entities whose identifies are presently unknown), Defendants, and DISNEY ENTERPRISES, INC.; MARVEL CHARACTERS, INC.; LUCASFILM LTD. LLC; and LUCASFILM ENTERTAINMENT COMPANY LTD. LLC, Interested Party Defendants.	Civil Action No. **DECLARATORY JUDGMENT COMPLAINT**

Plaintiff Capitol Specialty Insurance Corporation ("Capitol"), by and through its attorneys, Connell Foley LLP, as and for a Declaratory Judgment Complaint as to Defendants Characters for Hire, LLC ("Characters"); Nick Sarelli, a/k/a Avi Lieberman, d/b/a Characters for Hire, LLC ("Sarelli"); ABC Corporations 1-10 (individual fictitious corporate entities whose identifies are presently unknown) ("ABC Corporations"); and interested party Defendants Disney Enterprises, Inc. ("DEI"), Marvel Characters, Inc. ("Marvel"), and Lucasfilm Ltd. LLC and Lucasfilm Entertainment Company Ltd. LLC (collectively, "Lucasfilm"), alleges on knowledge as to its own acts and otherwise on information and belief as follows:

INTRODUCTION

1. This is a civil insurance coverage action for declaratory relief to determine the respective rights and obligations, if any, of Capitol, Characters, and Sarelli, under a policy of commercial liability insurance issued by Capitol to Characters (the "Policy") in connection with an underlying intellectual property infringement lawsuit filed by DEI, Marvel, and Lucasfilm.

2. In particular, Characters and Sarelli have asked Capitol to provide insurance coverage under the Policy in connection with the multi-count underlying lawsuit captioned *Disney Enterprises, Inc., Marvel Characters, Inc., Lucasfilm Ltd. LLC, and Lucasfilm Entertainment Company Ltd. LLC v. Avi Lieberman d/b/a Characters for Hire, LLC a/k/a www.charactersforhire.com and Nick Sarelli d/b/a Characters for Hire, LLC a/k/a www.charactersforhire.com*, pending in the United States District Court for the Southern District of New York, bearing Civil Action Number 1:16-cv-2340-GBD (the "Underlying Action").

3. As set forth in more detail herein, pursuant to the terms, conditions, and exclusions contained in the Policy, Capitol has agreed to pay for the defense of Characters and Sarelli in connection with the Underlying Action, subject to an express reservation of all rights under the Policy, in equity, and at law, including the right to seek declaratory relief concerning whether and to what extent Capitol is required to provide coverage under the Policy in connection with the Underlying Action and/or entitled to reimbursement of costs found attributable to non-covered claims.

4. The coverage issues give rise and will continue to give rise to an actual dispute and controversy between and among Capitol and Characters/Sarelli regarding the existence, scope, and extent of coverage, if any, available with respect to the Underlying Action under the Policy. Accordingly, Capitol respectfully brings this action seeking declaratory relief.

THE PARTIES

Declaratory Judgment Plaintiff

5. Plaintiff Capitol is a corporation organized under the laws of the State of Wisconsin having its principal place of business in Middleton, Wisconsin, and which is authorized to and does transact business in the State of New York.

Declaratory Judgment Defendants

6. Defendant Characters is a corporation organized under the laws of the State of Wyoming having its principal place of business in New York, New York, and which does transact business in the State of New York.

7. Defendant Sarelli is an individual residing in New Rochelle, New York, and who does transact business through Characters in the State of New York. Sarelli also transacts business through Characters by way of the fictitious name and pseudonym "Avi Lieberman."

8. Defendant ABC Corporations 1-10 are presently unknown fictitious corporate entities who are or may be liable to provide payments and/or insurance coverage for the matters alleged in the Underlying Action.

Interested Party Defendants

9. Interested Party Defendant DEI is a corporation organized under the laws of the State of Delaware having its principal place of business in Burbank, California.

10. Interested Party Defendant Marvel is an affiliate of DEI and a corporation organized under the laws of the State of Delaware having its principal place of business in Burbank, California.

11. Interested Party Defendants identified collectively as Lucasfilm are each affiliates of DEI and limited liability companies organized under the laws of the State of California having their principle place of business in Burbank, California.

12. Interested Party Defendants DEI, Marvel, and Lucasfilm (hereinafter referred to collectively as the "Underlying Plaintiffs") are included as nominal defendants in this action because they have or may have an interest in its outcome as plaintiffs in the Underlying Action.

JURISDICTION AND VENUE

13. There exists an actual and justiciable controversy between and among the parties concerning whether and to what extent insurance coverage may be available to Characters and Sarelli with respect to the Underlying Action under the Policy.

14. This Court has subject matter jurisdiction over this action pursuant to 28 U.S.C. § 1332 inasmuch as the parties have diverse citizenship and the alleged sum or value in controversy, exclusive of interest and costs, exceeds the amount of $75,000.

15. Venue is proper within the Southern District of New York pursuant to 28 U.S.C. § 1391(b) inasmuch as a substantial part of the events or omissions giving rise to this action took place in this District.

16. Personal jurisdiction exists over each of Defendants because Sarelli is resident domiciliary of the State of New York and the remaining Defendants transact business in and have otherwise submitted to jurisdiction in the State of New York.

THE UNDERLYING ACTION

17. The Underlying Plaintiffs have alleged in the Underlying Action that Characters and Sarelli infringed upon their copyrighted works and registered trademarks through the "advertising, marketing, promoting, producing, offering for sale, and selling themed character

entertainment party services" which allegedly incorporate the Underlying Plaintiffs' copyrighted works and registered trademarks without authorization.

18. The various alleged infringed-upon copyrighted works and registered trademarks are set forth at length in the Amended Complaint filed in the Underlying Action, a copy of which is annexed hereto as Exhibit A.

19. According to the Amended Complaint, the allegedly infringing activities include "paid character appearances at and for events such as children's parties and corporate gatherings" allegedly depicting or incorporating the Underlying Plaintiffs' copyrighted works and registered trademarks.

20. The Amended Complaint alleges that the Underlying Plaintiffs sent Sarelli letters dated November 24, 2015, December 9, 2015, and January 28, 2016, informing him of the alleged infringement and demanding that Characters and Sarelli cease and desist the allegedly infringing activities. Additionally, the November 24, December 9 and January 28 letters each sought damages from Characters and Sarelli, thereby constituting a "claim" against Characters and Sarelli within the meaning of the Policy by no later than November 24, 2015.

21. On or around December 10, 2015, Sarelli (using his pseudonym, Avi Lieberman) allegedly sent an email to counsel for the Underlying Plaintiffs stating that Characters and Sarelli had removed all infringing images from the Characters website and that "[i]t was not our intention to disregard the intellectual property rights of your client and we meant no harm in doing so." Nevertheless, the Amended Complaint asserts that Characters and Sarelli did not remove all allegedly infringing images and content from the Characters website and continue to engage in allegedly infringing activity.

22. The Underlying Plaintiffs filed a Complaint in the Underlying Action on March 30, 2016, followed by an Amended Complaint filed on June 24, 2016.

23. Although a claim had been asserted against Characters and Sarelli by November of 2015, and suit had been filed by March of 2016, Characters and Sarelli did not provide notice of an occurrence, offense, claim or suit to Capitol until May of 2016.

24. The Underlying Plaintiffs have included six counts in the Amended Complaint currently pending in the Southern District of New York:

i. **Count One** alleges ***copyright infringement*** in violation of 17 U.S.C. § 501, based upon Sarelli's allegedly willful, intentional and unauthorized commercial use of copyrighted works, including without limitation the unauthorized reproduction and/or copying, distribution and public display of intellectual property;

ii. **Count Two** alleges ***trademark infringement*** in violation of 15 U.S.C. § 1114, through Sarelli's prior and continued "use in commerce [of] unauthorized reproductions, copies, and/or colorable imitations of [the Underlying] Plaintiffs' [registered trademarks] in connection with the sale, offering for sale, distribution, and/or advertising of their services, which use[is] likely to cause confusion, mistake and/or deception among consumers";

iii. **Count Three** alleges ***unfair competition and false designation of origin*** under the Lanham Act, 15 U.S.C. § 1125, charging Sarelli's allegedly willful, intentional and unauthorized use of registered trademarks is "likely to cause confusion, deception, and mistake among the consuming public and trade as to the source, approval, connection, association, or sponsorship of the goods or services distributed, sold, and offered for sale by [Sarelli] bearing infringements of [the Underlying] Plaintiffs' [t]rademarks";

iv. **Count Four** alleges ***common law unfair competition***, based upon Sarelli's allegedly willful unauthorized use of registered trademarks, with the intention of "caus[ing] the public to believe that there is an affiliation or other association or connection between [the Underlying] Plaintiffs and [Sarelli], and/or between [the Underlying] Plaintiffs and [the party services], when in fact there is none";

v. **Count Five** alleges ***common law trademark infringement***, through Sarelli's allegedly "willful trademark infringement under the common law of the State of New York," through which Sarelli purportedly has made and continues to make substantial profits to which he is allegedly not entitled;

vi. **Count Six** alleges ***trademark dilution*** pursuant to New York General Business Law § 360-1, arising from Sarelli's averred dilution of the distinctive qualities of the Underlying Plaintiffs' registered trademarks, thereby causing harm to said Plaintiffs' business reputation.

25. Accordingly, in the Amended Complaint, the Underlying Plaintiffs seek, *inter alia*, the following equitable relief: to (1) permanently enjoin Sarelli from advertising, marketing, promoting, producing, offering for sale and/or selling party services incorporating their copyrighted works and registered trademarks, or from using their copyrighted works and

registered trademarks in any unauthorized manner; (2) direct that Sarelli cease the advertising, marketing, promoting, producing, offering for sale and/or selling of their party services incorporating their copyrighted works and registered trademarks on the Characters website and social media pages, as well as removing any references related thereto; (3) direct that the Underlying Plaintiffs' counsel be permitted to inspect and inventory Sarelli's warehouse to identify any and all infringing materials; (4) direct that Sarelli deliver any infringing merchandise in his and/or Characters' possession or under his and/or Characters' control to the Underlying Plaintiffs for destruction of same; and (5) direct "such other relief as the Court may deem appropriate to prevent the trade and public from gaining the erroneous impression that [the Underlying] Plaintiffs authorized or are related in any way to any goods or services advertised, marketed, promoted, offered for sale and/or sold by" Sarelli through Characters.

26. In addition to equitable relief, the Amended Complaint seeks federal statutory damages, including: (1) actual damages and/or Sarelli's profits, after an accounting, or statutory damages pursuant to 17 U.S.C. § 504(c) for each copyrighted work allegedly infringed; (2) three times the Underlying Plaintiffs' actual damages and/or Sarelli's profits, after an accounting, pursuant to 15 U.S.C. §§ 1125(a) and 1117(a); (3) the Underlying Plaintiffs' costs and reasonable attorneys' fees and investigative fees pursuant to 15 U.S.C. § 1117 and 17 U.S.C. § 505; and (4) exemplary and punitive damages under New York law, and any other such relief as the Court deems just and proper. Upon information and belief, the Underlying Plaintiffs are currently seeking only equitable relief and statutory damages and fees from Characters and Sarelli which damages and fees are not covered under the Policy.

THE CAPITOL POLICY

27. Capitol issued Commercial Liability Policy Number CS02542890-01 to Characters, which was in effect for the period June 24, 2015 to June 24, 2016 (previously and hereinafter referred to as the "Policy").

28. The Policy includes a commercial general liability coverage part (the "CGL Part") and was subsequently amended, effective September 25, 2015, to include an excess liability coverage part (the "Excess Part"). A copy of the Policy is annexed hereto as Exhibit B.

CAPITOL'S DEFENSE SUBJECT TO RESERVATION OF RIGHTS

29. Based upon the allegations in the Amended Complaint, Capitol has agreed to provide a defense to Characters and Sarelli under Coverage B of the CGL Part, which provides that Capitol will pay those sums that the insured becomes legally obligated to pay as damages because of "personal and advertising injury" to which the insurance applies, and that Capitol will have the right and duty to defend its insured against any suit seeking such damages, subject to the terms, conditions, provisions, and exclusions of the Policy.

30. In particular, the Policy defines "personal and advertising injury" to include injury arising out of the insured's conduct infringing upon another's copyright, trade dress, or slogan in the insured's "advertisement."

31. Because some, but not all, of the Underlying Plaintiffs' allegations in the Underlying Action refer to alleged infringement through advertising -- which allegations may potentially impact the Policy -- Capitol has agreed to provide a defense subject to an express reservation of rights pursuant to all terms, conditions, and exclusions therein, including the right to seek a judicial declaration concerning whether and to what extent Capitol may be obligated, if at all, to provide a defense and/or to indemnity in connection with the Underlying Action.

32. In particular, Capitol issued letters setting forth its coverage position, including a detailed reservation of rights and requests for information, through letters dated June 10, 2016, August 4, 2016, and September 28, 2016, copies of which are annexed hereto as Exhibits C, D, and E, respectively.

33. Based upon the allegations in the Underlying Action and the limited factual information that has been provided thus far, an actual justiciable controversy exists concerning the existence, nature, and scope of coverage, if any, that may be available in connection with the Underlying Action under the Policy.

COUNT ONE
(Declaratory Judgment - Existence, Scope and Extent of Coverage)

34. Capitol repeats, realleges, and incorporates by reference each of the allegations in Paragraphs 1 through 32 as if set forth fully and at length herein.

35. An actual controversy exists among the parties concerning the existence, scope and extent of coverage, if any, available to Characters and Sarelli with respect to the Underlying Action under the Policy.

36. Based upon the terms, conditions, provisions, and exclusions contained in the Policy, any coverage obligation owed by Capitol to Characters and/or Sarelli in connection with the Underlying Action is or may be barred or limited in whole or in part, including without limitation:

i. To the extent that the Underlying Action involves liability arising out of acts or omissions of an individual, organization, or entity other than those individuals, organizations, or entities listed as Named Insureds or otherwise qualifying as insureds under the Policy;

ii. To the extent that the Underlying Action involves injury found to have taken place prior to or otherwise outside the coverage period of the Policy;

iii. To the extent that the alleged injury is not "personal or advertising injury" or does not otherwise arise out of infringement upon another's copyright, trade dress, or slogan in an "advertisement" as the terms are used in the Policy;

iv. To the extent that Characters or Sarelli are found to have breached the notice and/or cooperation conditions of the Policy;

v. To the extent that Characters or Sarelli are found to have breached the condition in the Policy precluding an insured from voluntarily making a payment, assuming any obligation, or incurring any expense, other than for first aid, without Capitol's consent;

vi. To the extent that the Infringement of Copyright, Patent, Trademark, or Trade Secret exclusion is found to apply;

vii. To the extent that the Material Published Prior to Policy Period exclusion is found to apply;

viii. To the extent that the Material Published with Knowledge of Falsity exclusion is found to apply;

ix. To the extent that the Knowing Violation of Rights of Another exclusion is found to apply;

x. To the extent that the New York On Going Operations exclusion is found to apply;

xi. To the extent that the Contractual Liability exclusion is found to apply;

xii. To the extent that the Electronic Chatrooms or Bulletin Boards exclusion is found to apply;

xiii. To the extent that the Unauthorized Use of Another's Name or Product exclusion is found to apply;

xiv. To the extent that the Recording and Distribution of Material or Information in Violation of Law exclusion is found to apply;

xv. To the extent that the Other Insurance condition in the Policy is implicated;

xvi. To the extent that the Punitive or Statutory Damages exclusion is found to apply;

xvii. To the extent that the Amended Complaint seeks equitable relief which is not covered pursuant to the Policy; and

xviii. To the extent of all applicable limits of liability.

37. Because Characters and Sarelli have not presented the information alleged in the Underlying Action with sufficient particularity nor fully responded to Capitol's outstanding requests for information so as to make Capitol aware of all policy terms, conditions, provisions, exclusions, and/or other defenses which are or may become available so as to bar or limit coverage, Capitol reserves the right to amend this Declaratory Judgment Complaint and/or assert all applicable defenses if and when additional information becomes available.

38. In light of the foregoing coverage issues, Capitol respectfully requests a judicial determination from this Court concerning whether and to what extent Capitol is obligated, if at all, to provide insurance coverage to Characters and/or Sarelli in connection with the Underlying Action.

COUNT TWO
(Allocation and Apportionment as to Non-Covered Claims and Conduct)

39. Capitol repeats, realleges, and incorporates by reference each of the allegations in Paragraphs 1 through 37 as if set forth fully and at length herein.

40. Based upon the allegations in the Underlying Action, Capitol has agreed to provide a defense to Characters and Sarelli, subject to a reservation of rights, including the right to seek declaratory relief concerning whether and to what extent Capitol is required, if at all, to provide coverage under the Policy in connection with the Underlying Action.

41. In light of the foregoing coverage issues, Capitol respectfully requests a judicial declaration as to allocation and apportionment of costs and expenses attributable to non-covered claims, as well as injury arising from conduct happening during uninsured or other-insured periods for which Characters, Sarelli, and/or ABC Corporations 1-10 may be liable.

COUNT THREE
(Duty to Defend Subject to Coverage Determination)

42. Capitol repeats, realleges, and incorporates by reference each of the allegations in Paragraphs 1 through 40 as if set forth fully and at length herein.

43. Based upon the allegations in the Underlying Action, Capitol has agreed to provide a defense to Characters and Sarelli, subject to a reservation of rights, including the right to seek declaratory relief concerning whether and to what extent Capitol is required, if at all, to provide coverage under the Policy in connection with the Underlying Action.

44. In light of the foregoing coverage issues, Capitol respectfully requests a judicial declaration concerning whether and to what extent Capitol is required to continue providing a defense to Characters and Sarelli in connection with the Underlying Action pursuant to the terms, conditions, provisions, and exclusions in the Policy, and/or entitled to reimbursement of

defense costs and expenses incurred in connection with conduct and claims found not to be covered under the Policy.

COUNT FOUR
(Duty to Indemnify Subject to Coverage Determination)

45. Capitol repeats, realleges, and incorporates by reference each of the allegations in Paragraphs 1 through 43 as if set forth fully and at length herein.

46. Based upon the allegations in the Underlying Action, Capitol has agreed to provide a defense to Characters and Sarelli, subject to a reservation of rights, including the right to seek declaratory relief concerning whether and to what extent Capitol is required, if at all, to provide coverage under the Policy in connection with the Underlying Action.

47. In light of the foregoing coverage issues, Capitol respectfully requests a judicial declaration concerning whether and what extent Capitol is required to indemnify Characters and Sarelli in connection with the Underlying Action pursuant to the terms, conditions, provisions, and exclusions in the Policy.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff Capitol respectfully requests judgment and relief as follows:

A) A declaration determining the existence, scope, and extent of coverage, if any, with respect to the Underlying Action under the Policy;

B) A declaration of the parties' respective rights, obligations, and duties with respect to defense costs and/or indemnity payments made or to be made in connection with the Underlying Action, including but not limited to the obligation of Characters and/or Sarelli to pay for and/or reimburse Capitol for amounts attributable to non-covered claims;

C) For any and all declarations not expressly requested herein regarding the rights and duties of the parties that are necessary for the resolution of this matter; and

D) An award of Capitol's reasonable attorneys' fees and costs of this suit, and such other relief as this Court deems just, proper, and equitable.

CONNELL FOLEY LLP

Dated: New York, New York
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